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UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

FEDERAL TRADE COMMISSION, Plaintiff, vs. MEDLAB, INC., et al., Defendants.	Case No. CV-08-0822-SI DATE: July 18, 2008 TIME: 9 am CTRM: 10, 19th Floor

DEFENDANTS' OPPOSITION TO FTC'S MOTION TO STRIKE AFFIRMATIVE DEFENSES, JURY DEMAND AND NON-EXISTENT MOTION TO DISMISS

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INTRODUCTION

The FTC's Motion to Strike ten of Defendants' well-pled affirmative defenses should be denied because it attempts to eliminate factors highly relevant to the Court's determination of liability and the appropriateness and extent of any consumer or equitable relief. Although the FTC contends that the challenged affirmative defenses are deficient, the FTC has invoked equity in the Complaint and, as such, the principles of equitable jurisprudence should not be suspended. Further, the viability of a number of the affirmative defenses is dependent upon taking discovery, which has just begun.

This Court should recognize the Motion to Strike for what it is – a preemptive strike designed to foreclose the ability of Defendants to gather the very evidence needed to validate their defenses based on sound principles of equity. Defendants should be allowed a full and fair opportunity to litigate this case. It is well settled that a court should refuse to strike defenses unless they are unquestionably insufficient as a matter of law. The Motion to Strike should be denied and Defendants should be provided with a full hearing on the merits of their affirmative defenses after discovery concludes.

Additionally, Defendants are entitled to a jury trial based on the FTC's pre-trial disclosure which reveals that the FTC is ultimately seeking punitive relief.

Furthermore, the FTC's misplaced opposition to what it contends is a motion to dismiss should be denied. Defendants have not yet moved to dismiss, and their reference to such relief as part of the ultimate relief is plainly not a Local Rule 7.2 styled motion.

The FTC provides no authority for its procedural tactic, its claim is meritless, and should be denied.

I. A MOTION TO STRIKE AFFIRMATIVE DEFENSES IS DISFAVORED AND SHOULD BE DENIED

"Motions to strike should not be granted unless it is clear that the matter to be stricken could have no possible bearing on the subject matter of the litigation." *Colaprico v. Sun Microsystems, Inc.*, 758 F. Supp. 1335, 1339 (N.D. Cal. 1991) (*citing* 2A J. Moore, Federal Practice ¶ 12.21[2] at 2429 (2d ed.1975)); *see also Cal. Dep't of Toxic Substances Control v. Alco Pac., Inc.*, 217 F.Supp.2d 1028, 1033 (C.D. Cal. 2002) (motions to strike "generally regarded with disfavor because of the limited importance of pleading in federal practice, and because they are often used as a delaying tactic"); *Lazar v. Trans Union LLC,* 195 F.R.D. 665, 669 (C.D. Cal. 2000) (motions to strike "generally viewed with disfavor and are not frequently granted").

To strike an affirmative defense, the moving party carries the heavy burden of establishing: (1) there are no questions of fact; (2) any questions of law are clear and not in dispute; (3) **under no set of circumstances could the defense succeed**; and (4) presentation of the defense would prejudice the moving party. Schwarzer, Tashima & Wagstaffe, *Federal Civil Procedure Before Trial* §§ 9:381, 9:376, and 9:407 (2003) (emphasis added); *see also Hart v. Baca*, 204 F.R.D. 456, 457 (C.D. Cal. 2001).

The FTC bears an extraordinarily high burden on this Motion to Strike. *Advanced Microtherm, Inc. v. Norman Wright Mech. Equip. Corp.*, No. 04-02266, 2004 WL 2075445 at *12 (N.D. Cal. Sept. 15, 2004) (denying motion to strike portions of complaint). Importantly, the pleadings under attack are viewed in the light most favorable

to the pleader. *See Lazar v. Trans Union LLC*, 195 F.R.D. 665, 669 (C.D. Cal. 2000); *see also FTC v. Hang-Ups Art Enterprises, Inc.*, No. CV 95-0027 RMT, 1995 WL 914179 at *2 (C.D. Cal. Sept. 27, 1995). Moreover, a motion to strike will not be granted if the insufficiency of the defense is not clearly apparent, or if it raises factual issues that should be determined by a hearing on the merits. *FTC v. Medicor, LLC*, No. CV011896CBMEX, 2001 WL 765628 at *1 (C.D. Cal. June 26, 2001) (citing 5A C. Wright & A. Miller, *Federal Practice and Procedure*, §1381 at 678 (2d ed. 1990)).

II. DEFENDANTS' AFFIRMATIVE DEFNSES ARE MERITORIOUS

A. LACHES AND ESTOPPEL BASED ON THE FTC'S DELAY ARE EXPRESSLY ALLOWED AND REQUIRE A FACTUAL DETERMINATION AFTER DISCOVERY (Second Affirmative Defense)

The FTC is seeking to revisit decade-old conduct as evidenced by the discovery it has propounded relating to conduct dating back to 1996. *See, e.g.,* Lustigman Decl. at ¶¶1-2 (submitted herewith); Exs. 1(Request To Admit Nos.1 & 3) and 2 (Request For Production Nos. 24-26). Given that the FTC believes that decade-old conduct is relevant to this action sufficient to warrant affirmative discovery requests, Defendants are entitled to explore their laches and estoppel defenses.[1] If the advertising at issue is deceptive, as the FTC contends, why did the FTC sit on its hands for so long before coming into court seeking the extraordinary relief it now seeks?

While the FTC relies on the 1940 decision of *United States v. Summerlin*, 310 U.S. 414 (1940) to support its proposition that laches-type defenses cannot be applied against the government, there is more recent Supreme Court authority that expressly refused to rule that

[1] The sufficiency of Defendants' waiver defense discussed in Section G, *infra*.

the defense cannot be pled against the United States. *See Office of Personnel Management v. Richmond,* 496 U.S. 414, 423 (1990) ("We leave for another day whether an estoppel claim could ever succeed against the Government"). Moreover, in *SEC v. Randy*, 1995 WL 616788 (N.D. Ill. Oct. 17, 1995), the district court denied the SEC's motion to strike a laches defense because the applicability of laches is determined on a case-by-case basis and the defense is not inadequate as a matter of law: "The equitable defense of laches requires a lack of diligence on the part of the plaintiff and prejudice to the defendant from the delay" (citations omitted). *Id.* at *5.

Indeed, other California district courts have permitted the laches-type defense to go forward against the FTC and they should be permitted here. For example, in *FTC v. Hang-Ups Art Enters., Inc.,* 1995 WL 914179 at *4, the district court denied the FTC's Motion to Strike an identical laches defense, reasoning that the historical rule that laches is not available against the government may be subject to evolution, and the facts of each case should determine whether laches applies. *Id.* The *Hang-Ups* court explained that the Ninth Circuit's decision in *United States v. Ruby*, 588 F.2d 697, 705 n.10 (9th Cir. 1978) made clear that "laches may be a defense against the government if 'affirmative misconduct' by the government is shown." The *Hang-Ups* court ruled that "the facts of the case should decide whether there has been affirmative misconduct such that laches might apply" and refused to strike the affirmative defense. The *Hang-Ups* court ruling was followed by the district court in *FTC v. Braswell,* No. CV 03-3700 DT (PJWX)

(C.D. Cal. Nov. 10, 2003) at 13-14,[2] a case otherwise cited by the FTC, which allowed the laches defense to go forward to trial.[3]

While the *Hang-Ups* and *Braswell* decisions found that sufficient "affirmative misconduct" had been alleged, the Ninth Circuit and other courts have interpreted the term loosely and found that government inaction can qualify as affirmative misconduct without proof of "misfeasance." *See Yoo v. INS*, 534 F.2d 1325, 1329 (9th Cir. 1976) (inaction in the form of delay and failure to perform plain duty amounted to affirmative misconduct; "[j]ustice and fair play can only be achieved in this case by holding . . . that the Government is estopped from denying petitioner the benefit [he seeks]"); *Corniel-Rodriguez v. INS*, 532 F.2d 301, 306-307 (2d Cir. 1976) (failure to perform a legally required task found to amount to affirmative misconduct); *Beacom v. EEOC*, 500 F.Supp. 428, 438 (D. Ariz. 1980) ("whether nonfeasance by the Government is simply inaffirmative, or amounts to 'affirmative inaction' should be viewed with reference to the circumstances of each case").

Given the existence of a potential decade delay, Defendants are entitled to explore the basis of government inaction. Indeed, because there was a significant financial investment by the defendant companies in the research, development and marketing of

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[2]The *Braswell* decision which is cited in the FTC's motion to strike is attached to the Lustigman Declaration at Exhibit 3.

[3] Other recent decisions continue to recognize that the government may be equitably estopped from proceeding where the government has committed misconduct. *See Rumsfeld v. United Technologies Corp.*, 315 F.3d 1361, 1377 (Fed. Cir. 2003); *Zacharin v. United States*, 213 F.3d 1366, 1371 (Fed. Cir. 2000); *Linkous v. United States*, 142 F.3d 271 (5th Cir. 1998).

the products, which are it issue in this litigation, the government's delayed decision to bring an enforcement action prejudiced them. Defendants could have and would have altered the marketing and advertisements for the products at issue had the FTC filed an action earlier or advised that it considered the advertising to be false or unsubstantiated. These facts more than demonstrate the kind of prejudice which supports a laches defense. *See, e.g., Conopco, Inc. v. Campbell Soup Co.*, 95 F.3d 187 (2d Cir. 1996) (unreasonable delay of five years in the filing false advertising suit would have prejudiced the defendant); *Hot Wax, Inc. v. Turtle Wax, Inc.*, 27 F.Supp.2d 1043 (N.D. Ill.,1998), *aff'd*, 191 F.3d 813 (7th Cir. 1999); *see also Joint Stock Society v. UDV North America, Inc.*, 53 F.Supp.2d 692 (D.Del. 1999), *aff'd*, 266 F.3d 164 (3rd Cir. 2001).

Moreover, even the authority relied upon by the FTC in this argument permitted Defendants to assert the estoppel affirmative defense. *See FTC v. Magazine Solutions, LLC*, 2007 WL 2815695 at *1 (W.D. Pa. 2007) (denying motion to strike estoppel affirmative defense).[4] *See also Resolution Trust Corp. v. Gegor,* No. 94 CV 2578, 1995 WL 931093 at *3 (E.D.N.Y. Sept. 29, 1995) (denying government's motion to strike laches, waiver, and estoppel defenses); *FDIC v. Harrison*, 735 F.2d 408, 412 (11th Cir. 1984) (applying equitable estoppel to FDIC).

Defendants are thus entitled to pursue their defenses of laches and estoppel at this stage. Without such defenses, the FTC would be able to prosecute Defendants for conduct taking place a decade ago, which it appears it may be attempting here.

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[4] The unpublished *FTC v. Debt Solutions, Inc.* decision heavily relied upon by the FTC involved an *uncontested* motion to strike and should accordingly be discounted. 2006 WL 2257022 (W.D. Wash. 2006).

Defendants should be able to take discovery to more fully determine the extent laches and estoppel applies to the facts of this case. If the FTC delayed action, Defendants may have been significantly prejudiced. Given that Defendants' laches and estoppel defenses are sufficiently alleged, backed by a long period of inaction of on the part of the FTC, and have been permitted in other actions against the United States (including the FTC), the defenses should not be stricken here at this early stage of litigation.

B. THE FTC FAILED TO EXHAUST ADMINISTRATIVE REMEDIES (Third Affirmative Defense)

The FTC's failure to exhaust its administrative remedies should not be stricken as an affirmative defense because the Court should consider the FTC's actions when determining the propriety of granting an injunction. The Supreme Court has held that one of the requirements for injunctive relief has always been the inadequacy of legal remedies. *Weinberger v. Romero-Barcelo*, 456 U.S. 305, 311-312 (1982).

> The grant of jurisdiction to ensure compliance with a statute hardly suggests an absolute duty to do so under any and all circumstances, and a federal judge sitting as chancellor is not mechanically obligated to grant an injunction for every violation of law.

Id. at 313. Whether the FTC could have attained its stated goal of injunctive relief by pursuing less drastic means, such as by initiating administrative proceedings at any time during the period of alleged misconduct, is an issue that should be determined later in this case, and not be automatically ruled out by striking this affirmative defense. "An injunction is not the only means of ensuring compliance." *Id.* at 314.

Whether administrative remedies could have been pursued is material to the Court's determination on whether to grant an injunction.

C. THE FTC'S MAXIMUM RECOVERY IS CAPPED AT DEFENDANTS PROFITS, AND IN THE EVENT OF JUDGMENT IN THE FTC'S FAVOR, IT CAN RECOVER DEFENDANTS' PROFITS ONLY; DEFENDANTS ARE ENTITLED TO AN OFFSET OF ALL EXPENSES (Fourth and Twelfth Affirmative Defenses)

The FTC's statement on page 4 of its memorandum that "it is well settled that the amount of monetary relief in consumer protection cases brought under Section 13(b) of the FTC Act is equal to total consumer sales, less any refunds" is simply an incorrect statement of law. The law, as demonstrated by two recent circuit court decisions, has moved far away from the FTC's trumpeted position, and consequently, Defendants' fourth and twelfth affirmative defenses raise legal and factual issues that preclude them from being struck.

The FTC seeks the remedy of disgorgement in this action. However, the FTC's statutory grant of authority limits it equitable remedies, as opposed punitive remedies. Therefore, it is limited to disgorgement of profits, not disgorgement of revenues. *See FTC v. QT, Inc.*, 448 F.Supp.2d 908 (N.D. Ill. 2006), *aff'd*, 512 F.3d 858 (7th Cir. 2007).

Although the FTC argues against postage and taxes specifically, many offsets from a defendant's revenues are allowed in FTC cases, not just postage and taxes. *See FTC v. Verity Int'l, Ltd.*, 443 F.3d 48, 67 (2d Cir. 2006) (awarding "the full amount lost by consumers" can amount to reversible error); *FTC v. QT, Inc.*, 512 F.3d 858, 863 (7th Cir. 2008) (disgorgement of profits is the appropriate remedy).

In *Verity,* the district court was reversed for entering judgment in "the full amount lost by consumers." 443 F.3d at 67. The district court's award of $17.9 million in restitution was vacated by the Second Circuit because "[t]he appropriate measure for

restitution is the benefit unjustly received by the defendants." *Id.* (emphasis supplied). In remanding the case to the district court, the Second Circuit repeatedly emphasized that it was the defendants' unjust gain, not total gain that was relevant to the calculation of equitable restitution. *Id.* at 68 (focus of the restitution calculation should be on the defendants-appellant's unjust gains).

Similarly, *FTC v. QT, Inc.,* 448 F.Supp.2d 908 (N.D. Ill. 2006), *aff'd*, 512 F.3d 858 (7th Cir. 2008) supports the viability of the affirmative defense of offset. Rejecting the FTC's demand for the defendant's gross revenues, the *QT* court ordered the disgorgement of defendants' profits and also ordered that every purchaser should be offered a refund. 448 F.Supp.2d at 975.

In *FTC v. Figgie International, Inc.,* 994 F.2d 595 (9th Cir. 1993), an FTC case brought under section 19(b) of the FTC Act and relied by the FTC in its brief on this issue, the Ninth Circuit wrote that "if disgorgement of Figgie's receipts would exceed redress to consumers, then in the circumstances of this case requiring Figgie to pay the Commission the excess would be for the purpose of punishing Figgie, not making redress to the consumers who bought [the product]. Not all the receipts for [the product] need to be the result of deceptive practices, because the Commission found that the [product] had value, might reasonably have been purchased by some consumers, and that some of the claims made for them in the promotional materials were true." *Id.* at 607.

Moreover, while the FTC places great weight on the *Bronson* decision, this exact issue was decided against the FTC in that case there when its motion to strike the affirmative defense of offset was denied. *See FTC v. Bronson Partners, LLC,* No. 3:04CV1866(SRU), 2006 WL 197357 at *2 (D. Conn. Jan. 25, 2006) (declining to strike

affirmative defenses because "any monetary award may reflect benefits received by consumers....") .

These decisions are by no means unique. In *Braswell* (issued even prior to the *Verity* and *QT* decisions which recognized offsets), the court denied the FTC's motion to strike the affirmative defense stating:

> this Court finds that a determination as to the applicability of this affirmative defense is premature. In other words, the law that an offset/setoff is not allowed is not "beyond dispute." In fact, while the FTC argues that *no* deductions are proper, the FTC's own case law demonstrates that the types of "offset/setoff" sought by Defendants are frequently deducted from overall judgments.

FTC v. Braswell (Lustigman Decl., Ex. 3) at 17-18.

Moreover, under other recent decisions, FTC restitution claims were limited to a defendant's profits and also offset by the value conferred upon consumers.[5] Indeed, in the specific context of FTC cases, courts have found that a defendant's revenues are not the proper basis for damages awarded under the FTC Act. Many courts either refused to award damages or offset the damages claimed by the FTC when consumers are conferred some type of benefit from their dealings with a defendant. In *FTC v. Magui Publishers, Inc.*, Civ. No. 89-3818 RSWL(GX), 1991 WL 90895 at *12 (C.D. Cal. Mar. 28, 1991), *aff'd,* 9 F.3d 1551 (9th Cir. 1993), the court deducted from the damages award the defendants' costs of producing falsely advertised Dali etchings and lithographs.

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[5] Courts routinely deduct amounts that plainly reduce the wrongdoer's actual profit from governmental recoveries, such as expenses and transaction costs. *SEC v. Lorin*, 76 F.3d 458, 462 (2d Cir. 1996) ("the decision to order disgorgement of ill-gotten gains, and the calculation of those gains, lie within the discretion of the trial court, which must be given wide latitude in these matters"); *SEC v. Blatt*, 583 F.2d 1325, 1335 (5th Cir. 1978) (disgorgement is remedial, not punitive).

> Thus, the defendants' gross revenue, and the amount of consumer injury, from their illegal activity earned was at least $3.96 million [...] The sum of the costs for lithographs and etchings would then equal roughly $2.0 million. When this cost figure is subtracted from the defendants' revenue, previously calculated to be $3.96 million, the amount of unjust enrichment to the defendants is determined to be $1.96 million.

Id. In *FTC v. Kuykendall*, 371 F.3d 745, 766-67 (10th Cir. 2004), the defendants' gross receipts were used merely as a baseline to establish restitution amount.

Accordingly, should the FTC prevail, the amount of the offset that should be deducted from total revenues is an important issue in this case and is far from "spurious" as the FTC claims. The fourth and twelfth affirmative defenses therefore should not be stricken.

D. TRUTHFUL COMMERCIAL SPEECH WARRANTS FIRST AMENDMENT PROTECTION (Fifth Affirmative Defense).

The FTC's attempt to strike Defendants' fifth affirmative defense[6] should be denied as it is bsed on decisional authority that pre-dates the landmark ruling in *Pearson v. Shalala*, 164 F.3d 650, 655 (D.C. Cir. 1999) and otherwise ignores other important decisions supporting the defense.

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[6] Defendants' fifth affirmative defense provides: "This Complaint is barred because the Defendants' actions are privileged and protected by the First Amendment to the United States Constitution. The FTC, by its Complaint, seeks to restrict, restrain and/or prohibit protected commercial speech, through the use of ad hoc and non-defined terms and advertising substantiation lacking any measurable degree of definiteness. To the extent the FTC's actions are premised upon alleged representations made "by implication", the FTC has labeled them false or misleading without relying on extrinsic evidence. In proceeding this way, the FTC has failed to choose and/or rejected all alternate means of achieving its interests that are less restrictive of protected speech."

It cannot be disputed that truthful commercial speech is protected by the First Amendment. *Central Hudson Gas & Electric Corp., v. Public Service Commission of New York,* 447 U.S. 557 (1980). In this action, the FTC goes beyond merely challenging untrue commercial speech – but instead focuses on the level of substantiation it contends must be possessed for dietary supplement advertising to be considered truthful commercial speech. Courts have recognized that FTC standards regarding advertising can be challenged on First Amendment grounds. *See, e.g., Beneficial Corp. v. FTC*, 542 F.2d 611, 618-20 (3rd Cir. 1976) (allowing First Amendment challenge to FTC's total ban on the use of certain phrase in advertising tax preparation). Indeed, in *Pearson, supra,* the District of Columbia Circuit rejected as "almost frivolous" an almost identical argument by the government ruling "that health claims lacking 'significant scientific agreement' are inherently misleading and thus entirely outside the protection of the First Amendment." 164 F.3d at 655.

Similarly, the district court in *FTC v. Bronson* recognized the availability of the First Amendment to the advertising of dietary supplement products. *See FTC v. Bronson,* 2006 WL 197357 at *2 (permitting First Amendment defense to go forward as "there may be a set of facts that support the defendants' claim that their actions are protected by the First Amendment"). In fact, even the FTC's own administrative tribunal has recognized that defendants should be entitled to develop a record on First Amendment issues. *See In the Matter of Basic Research, L.L.C.,* FTC Docket No. 9318, 2004 WL 2682854 (F.T.C.) (Nov. 4, 2004) at p.3 (First Amendment defense relating to substantiation must be deferred until factual record has been developed).

Defendants' First Amendment related defenses are entitled to go forward so that they may demonstrate the merits of the scientific basis behind its advertising claims. Commercial speech explaining the scientific evidence is protected by the First Amendment as long as it is truthful and not misleading.

E. THE FTC HAS FAILED TO PROVIDE FAIR NOTICE OF WHAT CONSTITUTES A "REASONABLE BASIS" (Sixth Affirmative Defense)

Remarkably, the FTC argues that Defendants' Constitutional due process rights[7] relating to the FTC's standards of "reasonable" substantiation is "spurious" and "defies credulity." Perhaps caught up in its attempt at limiting Defendants' constitutional rights to study the basis of the defense, the FTC fails to advise the Court that such a defense serves the basis for the leading jurisprudence on dietary supplement claims and has otherwise been recognized by its own tribunal.

In *Pearson v. Shalala, supra*, the appropriateness of the "due process" clause of the Fifth Amendment was recognized in considering the vague standards utilized by the FDA in restricting claims relating to dietary supplement products. *See Pearson, supra,*

[7] Defendants' sixth affirmative defense provides: "This action is based upon regulatory standards governing the quantity and quality of substantiation Defendants must possess at the time they make express and implied claims in advertisements. The standards fail and have failed to provide reasonable persons, including Defendants, with fair notice as to whether contemplated claims in advertisements, including those at issue in this proceeding, are and were permissible and/or allow and have allowed the FTC and/or its representatives to enforce the standards pursuant to their personal or subjective predilections. The regulatory standards are thus unconstitutionally vague on their face and/or as applied to Defendants' prior and contemplated advertising activity and, therefore, violate Defendants' rights to due process under the Fifth Amendment to the Constitution of the United States and the Complaint is thus not in the public interest. The Complaint based upon such standards is therefore barred.

164 F.3d at 660 (FDA's requiring "significant scientific agreement" fails to provide dietary supplement companies with sufficient guidance was "squarely" presented on Fifth Amendment vagueness challenge). The D.C. Circuit thereafter declared the FDA regulations invalid because they failed to put dietary supplement companies on notice as to the principles guiding agency action and to set forth the FDA's meaning of "significant scientific agreement" or "at minimum, what it does not mean." *Id.* at 661.

Similarly, the FTC's own administrative tribunal denied its counsel's motion to strike a due process affirmative defense. *See Basic Research,* 2004 WL 2682854 (F.T.C.) at pp.2-3 (denying motion to strike due process defense so that factual record can be developed).

At bar, Defendants intend to challenge the FTC's vague standards that it utilizes to support its "reasonable basis" standard for dietary supplement health claims. The current standard fails to give dietary supplement marketers sufficiently defined standards as to what "reasonable basis" means or doesn't mean. While the FTC will likely assert in this litigation that its "reasonable basis standard" means only double-blind, placebo controlled clinical human testing for making a claim, such a standard is not published through formal procedures and has otherwise been rejected by the Ninth Circuit. *See, e.g., FTC v. Enforma Natural Products, Inc.*, 362 F.3d 1204, 1217 (9th Cir. 2004) (rejecting FTC's position that only double-blind, placebo controlled clinical testing could serve to substantiate dietary supplement weight loss' claims). The rejection of the FTC's standard was again affirmed over the FTC's objections earlier this year:

> Nothing in the Federal Trade Commission Act, the foundation of this litigation, requires placebo-controlled, double-blind studies. The Act

> forbids false and misleading statements, and a statement that is plausible but has not been tested in the most reliable way cannot be condemned out of hand. The burden is on the Commission to prove that the statements are false.

FTC v. QT, Inc., 512 F.3d 858, 861 (7th Cir. 2008).

Given that there FTC lacks a defined standard of reasonable basis, it has failed to put Defendants on notice as to what it considers a reasonable basis for a dietary supplement advertising claim. Defendants are entitled to explore the lack of such standards in discovery and to present at trial evidence demonstrating that the failure to provide such standards warrants a finding of void for vagueness.

F. DEFENDANTS MAY CHALLENGE THE FTC'S ARBITRARY AND CAPRICIOUS STANDARD (Sixth & Thirteenth Affirmative Defenses)

The FTC does not have unlimited discretion to seek enforcement against one company that it has not sought against other competitors who may have committed similar violations of the law. *See FTC v. Universal-Rundle Corp.*, 387 U.S. 244, 251 (1967) (FTC "does not have unbridled power to institute proceedings which will arbitrarily destroy one of many law violators in an industry"). Other courts have followed this admonition and have not permitted arbitrary enforcement. *See, e.g., Johnson Product Co. v. FTC*, 549 F.2d 35 (7th Cir. 1977) (remanding to FTC for consideration of differences in consent orders negotiated with competitors); *Ford Motor Co. v. FTC,* 547 F.2d 954 (6th Cir. 1976) (comparing requirements in consent decree entered into by General Motors to consent decree entered into by Ford to ascertain whether Ford would be placed in competitive disadvantage), *cert. denied*, 431 U.S. 915 (1977); *Diener's Inc. v. FTC*, 494 F.2d 1132, 1133 (D.C. Cir. 1974) (modifying consent

decree so that restrictions would be same as those entered into by competitor).

At bar, the FTC's failure to establish defined and understandable standards for advertisers is a critical flaw and Defendants should be entitled to demonstrate that the FTC seeks relief in this action that it has not sought against other dietary supplement and health product marketers accused of false claims or lack of substantiation. By striking these affirmative defenses, the Court would effectively be imposing a rule mandating that Defendants prove this element of this case before discovery has been completed. Given that the evidence of inconsistent enforcement lies in the hands and files of the FTC, such a burden would be impossible. Defendants are entitled to explore why the FTC is taking a position against Defendants that is inconsistent with the relief sought in prior cases.

G. BECAUSE THE PRODUCTS WERE SOLD WITH A MONEY BACK GUARANTEE OF SATISFACTION, CONSUMER WAIVER IS A PROPER AFFIRMATIVE DEFENSE TO A CLAIM OF CONSUMER REDRESS (Ninth Affirmative Defense)

The FTC seeks to preclude Defendants from asserting a waiver defense. However, the waiver defense should not be stricken for two independent reasons: (a) each allegedly injured consumer may have waived their rights to seek restitution because he or she entered into a valid and binding contract to purchase the product at issue, and the contract defined the terms under which redress could be obtained. The products at issue were sold with a money-back guarantee of satisfaction, and there is no allegation that the guarantee was dishonored or that any dissatisfied consumer was denied a refund if requested. Just as the FTC is not precluded from exploring whether the money-back guarantee was dishonored, Defendants should not be prevented from asserting that guarantee was in fact honored, and therefore consumers have waived certain other rights to obtain relief; and

(b) by years of inaction before filing suit and challenging conduct that is up to a decade old, the FTC may have had every opportunity to request that Defendants change their practices but the FTC chose to remain silent. Defendants are entitled to explore what the FTC knew and when it knew it, and whether principles of equity preclude the FTC from asserting claims it may have knowingly decided not to press in the past.

The FTC's bid to strike this defense is contrary to the decisions of other courts. On the issue of consumer waiver, the FTC stands in the shoes of each consumer and it is a question of fact whether consumers waived their claims. The FTC should not intrude into contracts entered into by individual parties absent fraud.

For example, the Eleventh Circuit refused to strike a similar defense and allowed such a defense to be asserted against a branch of the federal government in *FDIC v. Harrison*, 735 F.2d 408 (11th Cir.1984). "We see no reason not to apply the traditional rules of equitable estoppel to the conduct of FDIC". *Id.* at 412. In *U.S. v. Walerko Tool and Engineering Corp.*, 784 F.Supp. 1385, 1389 (N.D. Ind. 1992), the district court refused to strike a waiver defense against the government because a question of fact existed as to whether the government waived its claims. In *Resolution Trust Corporation v. Gregor*, 1995 WL 931093 at *3, the court found the viability of laches, estoppel and waiver defenses to be an open and disputed question and declined to decide the issue on a motion to strike. Accordingly, the plaintiff's motion to strike was denied, and the same result should issue in the motion at bar.

H. THE CHALLENGED CLAIMS HAVE CEASED, SO THE FTC'S REQUESTS FOR INJUCTIVE RELIEF ARE MOOT (Eleventh Affirmative Defense)

Contrary to the FTC's assertions, the affirmative defense of mootness is valid. As a general matter, "[p]ast wrongs are not enough for the grant of an injunction." *FTC v. Sage Seminars, Inc.*, No. C 95-2854 SBA, 1995 WL 798938 at *6 (N.D. Cal. Nov. 2, 1995); *Enrico's Inc. v. Rice*, 730 F.2d 1250, 1253 (9th Cir. 1984).

Claims for injunctive relief may be moot if the defendant can show that there is no reasonable expectation that the wrongful conduct will be repeated. *United States v. W.T. Grant Co.*, 345 U.S. 629, 633 (1953); *SCM Corp. v. FTC*, 565 F.2d 807, 812 (2d Cir. 1977). Although cessation of the conduct at issue does not foreclose injunctive relief or automatically render a case moot, this principle does not preclude the Defendants from even raising a defense of mootness.

Court's have recognized the availability of the defense in FTC actions particularly as it relates to the appropriateness of the remedy. Indeed, in the decision frequently cited by the FTC at bar, *FTC v. Bronson*, *supra*, the district court refused to strike the mootness affirmative defense. *Bronson*, *supra*, 2006 WL 197357 at * 3 ("Although cessation of conduct is not a defense to a violation of the FTC Act, like the good faith defense, it may be relevant with respect to an appropriate remedy."); *see also FTC v. Affordable Media, LLC*, 179 F.3d 1228, 1238 (9th Cir. 1999) (*citing United States v. Concentrated Phosphate Export Ass'n, Inc.*, 393 U.S. 199, 203 (1968)). While the Supreme Court also said that "the test for mootness [...] is a stringent one" (*Id.*), this does not preclude Defendants from asserting the defense and attempting to meet their burden of proof.

Here, the business practices challenged by the FTC have ceased and are not likely to continue. The case law clearly allows a defense of mootness where a defendant meets the required burden. *See W.T. Grant Co., supra,* 345 U.S. at 633. Certainly, Defendants' cessation of conduct prior to the initiation of this action is relevant to the appropriateness of any relief and Defendants should not be barred from raising this defense.

I. INJNUNCTIVE RELIEF SHOULD NOT ISSUE DUE TO THE PRESENCE OF AN ADEQUATE REMEDY AT LAW (Tenth Affirmative Defense)

The FTC seeks to strike Defendants' tenth affirmative defense that: "Plaintiff is not entitled to consumer relief because there exists an adequate remedy at law" despite the fact that it is seeking monetary recovery in the guise of ancillary equitable relief.

The Court should consider this affirmative defense when it determines whether to grant any ancillary equitable monetary relief. *See FTC. v. Evans Products Co.,* 775 F.2d 1084, 1087 (9th Cir. 1985) ("in the absence of ancillary relief, Evan's customers may still obtain relief through state actions tailored to the specific misrepresentations alleged in their individual cases"). Since the FTC seeks ancillary relief, the Defendants' affirmative defense that such relief provides an adequate remedy at law should not be stricken.

III. DEFENDANTS ARE ENTITLED TO A JURY TRIAL TO THE EXTENT THE FTC SEEKS A PUNITIVE REMEDY OR ANCILLARY MONETARY RELIEF

Defendants seek a right to trial by jury on each of the claims to the extent the FTC is seeking legal, not equitable relief. Despite pleading a request for ancillary monetary relief, demanding joint and several liability, and providing a damage calculation in discovery that is penal in its relief, the FTC claims that Defendants should be stripped of

their Seventh Amendment right to a jury trial. An examination of the Complaint reveals that the FTC is seeking remedies well beyond purely equitable relief. In Paragraph 20 of the FTC's Complaint, the FTC asserts that, in addition to equitable relief, it is seeking additional "ancillary relief" which essentially amount to monetary damages.

The FTC's request for ancillary monetary relief clearly goes beyond pure equity. By claiming an entitlement to a damage award in the amount of gross sales (less merely refunds and chargebacks), the FTC is seeking a penal remedy. From the perspective of the individual defendant Holmes, the FTC is seeking a damage award well in excess of monies he received. Thus, such a demand is plainly penal in nature as recognized by the Ninth Circuit authority relied upon by the FTC. *See FTC v. Figgie International, Inc.*, 994 F.2d 595 (9th Cir. 1993). Moreover, even though Defendants would have paid significant portions of revenue to the United States Treasury in the form of taxes and any damage relief here, if obtained, will more than likely go to the United States Treasury as opposed to consumers.[8] Given that the FTC's demand seeks effectively a double payment to the United States Treasury, the FTC is in effect seeking to assess a penalty. Separate from the merits of such a claim, the FTC's formal intention to seek such relief triggers Defendants' constitutional right to a trial by jury.[9]

It is well-settled that a jury is guaranteed under the Seventh Amendment to the Constitution when the relief sought is legal in nature.

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[8] Upon information and belief, discovery will likely reveal that a significant portion of damages obtained by the FTC in the name of "consumer redress" actually ends up in the general fund of the United States Treasury, and not in the hands of consumers.

[9] The FTC fails to make any showing of how it would be prejudiced by having its claims tried by a jury.

> [I]f a "legal claim is joined with an equitable claim, the right to jury trial on the legal claim, including all issues common to both claims, remains intact. The right cannot be abridged by characterizing the legal claim as 'incidental' to the equitable relief sought." *Curtis v. Loether,* 415 U.S., at 196, n. 11, 94 S.Ct., at 1009, n. 11. Thus, petitioner has a constitutional right to a jury trial to determine his liability on the legal claims.

Tull v. United States, 481 U.S. 412, 425 (1987).

Here, the monetary relief requested as to Defendants is akin to a legal damages claim, given that the FTC is seeking Defendants' total revenues, not just their alleged unjust gains.

In FTC cases, issues of liability and monetary damages have been bifurcated for separate determinations. *See FTC v. Minuteman Press, LLC,* 53 F.Supp.2d 248, 251 (E.D.N.Y. 1998). The Court can elect to use that option in this case. Thus, Defendants are entitled to have a jury decide if there is any liability for the monetary relief being sought by the FTC.

IV. THE FTC'S OPPOSITION TO A NON-EXISTENT MOTION TO DISMISS SHOULD BE DENIED

Although Defendants have not moved to dismiss, the FTC has filed an opposition to what it inexplicably views as a motion to dismiss – Defendants' prayer for relief. In Defendants' prayer for relief, Defendants seek, *inter alia*, dismissal of the complaint with prejudice. While this is a proper request for ultimate relief, the FTC provides no authority that a prayer for relief should be consider a motion under Local Rule 7.2 and F.R.C.P. Rule 12(b). Having created a strawman motion to dismiss, the FTC's attempt defeat a motion that Defendants have not made should be denied.

CONCLUSION

The FTC's Motion to Strike and Opposition to a Non-Existent Motion to Dismiss should be denied on all grounds set forth above.

Dated: June 19, 2008

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CERTIFICATE OF SERVICE

I, Marie Carney, a paralegal at The Lustigman Firm, P.C., counsel for the defendant in the within action, do hereby certify that true and correct copies of the following documents:

DEFENDANT'S OPPOSITION TO FTC'S MOTION TO STRIKE AFFIRMATIVE DEFENSES, JURY DEMAND AND NON-EXISTENT MOTION TO DISMISS

AFFIDAVIT OF ANDREW B. LUSTIGMAN

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